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UNITED STATES GENERAL ACCOUNTING OFFICE  
WASHINGTON, D.C. 20548

FOR RELEASE ON DELIVERY  
EXPECTED AT 10 A.M. EDT  
TUESDAY, JANUARY 22, 1974

SUMMARY STATEMENT OF  
BALTAS E. BIRKLE, DEPUTY DIRECTOR  
RESOURCES AND ECONOMIC DEVELOPMENT DIVISION  
UNITED STATES GENERAL ACCOUNTING OFFICE  
BEFORE THE  
CONSERVATION AND NATURAL RESOURCES SUBCOMMITTEE  
OF THE  
COMMITTEE ON GOVERNMENT OPERATIONS  
HOUSE OF REPRESENTATIVES  
ON  
PROPOSED POWER RATE INCREASE  
BY THE BUREAU OF RECLAMATION'S  
CENTRAL VALLEY PROJECT

MR. CHAIRMAN AND MEMBERS OF THE SUBCOMMITTEE:

WE ARE PLEASED TO APPEAR TODAY AT THE REQUEST OF THE SUBCOMMITTEE TO DISCUSS OUR REPORT ON THE PROPOSED JANUARY 1974 POWER RATE INCREASE FOR THE BUREAU OF RECLAMATION'S CENTRAL VALLEY PROJECT IN CALIFORNIA. OUR REVIEW WAS MADE PURSUANT TO YOUR LETTER TO THE COMPTROLLER GENERAL OF JULY 24, 1973, AS MODIFIED BY SUBSEQUENT DISCUSSIONS WITH YOUR OFFICE WHICH REQUESTED US TO EVALUATE THE REASONABLENESS OF 11 CONTENTIONS MADE BY OPPONENTS OF THE BUREAU'S PROPOSED 51.6-PERCENT POWER RATE INCREASE FOR THE CENTRAL VALLEY PROJECT.

THE REPORT ON THE RESULTS OF OUR REVIEW WAS PRESENTED TO THE SUBCOMMITTEE ON NOVEMBER 19, 1973 (B-125042). WITH YOUR PERMISSION, MR. CHAIRMAN, I WOULD LIKE, AT THIS TIME, TO SUBMIT FOR THE RECORD A COPY OF THE REPORT AND A COPY OF OUR RESPONSE TO THE ADDITIONAL

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MATTERS REQUESTED IN YOUR LETTER DATED NOVEMBER 20, 1973, TO THE COMPTROLLER GENERAL. MY ORAL STATEMENT THIS MORNING WILL BRIEFLY SUMMARIZE THE REPORT.

THE BUREAU'S CENTRAL VALLEY PROJECT CONSISTS OF A NUMBER OF DAMS AND RELATED WATER CONVEYANCE SYSTEMS, HYDROELECTRIC GENERATING PLANTS, AND TRANSMISSION FACILITIES. THE PROJECT PROVIDES IRRIGATION WATER, MUNICIPAL AND INDUSTRIAL WATER, POWER GENERATION, FLOOD CONTROL, AND FISH AND WILDLIFE ENHANCEMENT. COSTS OF THE PROJECT ALLOCATED TO POWER ARE REQUIRED TO BE RECOVERED IN RATES CHARGED POWER CUSTOMERS AND TO BE REPAYED TO THE U.S. TREASURY. INTERIOR USES 50 YEARS FROM THE DATE A HYDROELECTRIC PLANT IS PLACED IN SERVICE AS A REASONABLE REPAYMENT PERIOD.

TO DETERMINE WHETHER POWER RATES ARE ADEQUATE FOR RECOVERING THE FEDERAL INVESTMENT WITHIN THE REQUIRED REPAYMENT PERIOD, EACH FEDERAL POWER MARKETING AGENCY GENERALLY MAKES AND PERIODICALLY PUBLISHES CONSOLIDATED RATE AND REPAYMENT STUDIES. THESE STUDIES SHOW ACTUAL COSTS AND REVENUES THROUGH THE CURRENT FISCAL YEAR AND PROJECTED COSTS AND REVENUES THROUGH THE REMAINDER OF THE REPAYMENT PERIOD.

SOME OF THE CONTENTIONS MADE BY THE OPPONENTS OF THE PROPOSED 51.6-PERCENT RATE INCREASE INVOLVE SUGGESTIONS WHICH WOULD REQUIRE AGREEMENT BETWEEN THE BUREAU OF RECLAMATION AND THE PACIFIC GAS AND ELECTRIC COMPANY. BECAUSE WE CANNOT PREDICT THE TERMS THAT WOULD BE INVOLVED IN SUCH AN AGREEMENT, WE HAVE NOT MADE A CONCLUSION AS TO THE VALIDITY OF THESE CONTENTIONS. WE WOULD QUESTION, HOWEVER, THE WISDOM

OF PREPARING RATE AND REPAYMENT STUDIES BASED ON PREDICTING CHANGES IN OPERATING METHODS THAT ARE SUBJECT TO THE OUTCOME OF FUTURE AGREEMENTS BETWEEN THE BUREAU OF RECLAMATION AND PACIFIC GAS AND ELECTRIC.

IN OUR OPINION, HOWEVER, 4 OF THE 11 CONTENTIONS HAD MERIT. THESE FOUR CONTENTIONS--NUMBERED 2, 6, 7, AND 10 IN YOUR JULY 24, 1973, LETTER TO US--CONCERNED HYDROLOGY STUDIES, EARNED SURPLUS, REPLACEMENT COSTS, AND THE NO-DEFICIT-YEAR CONCEPT. THREE OF THESE FOUR CONTENTIONS INVOLVE RATE AND REPAYMENT STUDY PROCEDURES WHICH THE BUREAU OF RECLAMATION COULD CHANGE UNILATERALLY AND ONE INVOLVED USING UPDATED HYDROLOGY STUDIES. IF THE BUREAU WERE TO CHANGE ITS RATE AND REPAYMENT STUDY TO RECOGNIZE THESE FOUR CONTENTIONS, IT WOULD TEND TO REDUCE SUBSTANTIALLY THE AMOUNT OF THE PROPOSED RATE INCREASE.

NO-DEFICIT-YEAR CONCEPT--CONTENTION 10

THE CONTENTION INVOLVING THE NO-DEFICIT-YEAR CONCEPT IS THAT THE BUREAU IS UNJUSTIFIED IN INCREASING POWER RATES STARTING IN 1974 TO A LEVEL THAT WILL PRODUCE NO DEFICIT IN ANY SINGLE YEAR FROM 1974 TO 2031. UNDER THIS CONCEPT A POWER RATE IS ESTABLISHED WHICH IS ESTIMATED TO BE AT LEAST ADEQUATE TO PROVIDE REVENUES IN EACH YEAR OF THE REMAINING REPAYMENT PERIOD (1974-2031) TO PAY ALL OPERATION AND MAINTENANCE EXPENSES, THE INTEREST EXPENSE, THE PURCHASE POWER COST, AND THE REPLACEMENT COST. WE WERE TOLD THAT THIS CONCEPT WAS ESTABLISHED FOR ONLY THE CENTRAL VALLEY PROJECT. IF POWER RATES ARE ESTABLISHED FOR THE ENTIRE REPAYMENT PERIOD ON THE BASIS OF AVOIDING A DEFICIT IN EVERY YEAR INCLUDING YEARS WITH ABNORMALLY HIGH EXPENSES, THE RESULT CAN BE

POWER RATES WHICH PROVIDE SUBSTANTIALLY EXCESSIVE POWER REVENUES IN OTHER THAN ABNORMAL YEARS. ACCORDING TO BUREAU REGIONAL OFFICIALS, THE NO-DEFICIT-YEAR CONCEPT WAS PRIMARILY RESPONSIBLE FOR THE NEED FOR THE INCREASED POWER RATES WHICH WOULD RESULT IN AN ESTIMATED SURPLUS OF ABOUT \$496 MILLION AT THE END OF THE REPAYMENT PERIOD.

WE BELIEVE THAT THE NO-DEFICIT-YEAR CRITERION IS INCONSISTENT WITH THE REPAYMENT POLICY SET FORTH IN AN APRIL 1, 1966, REPORT<sup>1</sup> BY THE HOUSE COMMITTEE ON INTERIOR AND INSULAR AFFAIRS.

THE HOUSE REPORT RECOGNIZED THAT OPERATING COSTS AND REVENUES MIGHT VARY FROM YEAR TO YEAR AND POINTED OUT THAT THE INTENDED APPROACH TO REPAYMENT SCHEDULING "HAS THE EFFECT OF AVERAGING THE YEAR-TO-YEAR VARIATIONS IN COSTS AND REVENUES OVER THE REPAYMENT PERIOD." IN OUR OPINION, THE NO-DEFICIT-YEAR CONCEPT USED IN THE RATE AND REPAYMENT STUDY IS INCONSISTENT WITH THIS "AVERAGING" APPROACH TO REPAYMENT.

THE BUREAU'S REGIONAL OFFICE MADE A STUDY IN WHICH IT INDICATED THAT IF THE NO-DEFICIT-YEAR CONCEPT WERE ELIMINATED AND IF A SURPLUS WERE PROVIDED WHICH WAS APPROXIMATELY ADEQUATE TO COVER \$78.4 MILLION IN DEFERRED COSTS DISCUSSED UNDER CONTENTION 6, THE EFFECTIVE NET POWER RATE FOR THE CENTRAL VALLEY PROJECT WOULD BE 5.55 MILLS, RATHER THAN THE PROPOSED 6.15 MILLS, PER KWH. THE PRESENT NET POWER RATE IS 4.08 MILLS PER KWH. A POWER RATE OF 5.55 MILLS WOULD REPRESENT ABOUT A 36-PERCENT RATE INCREASE COMPARED WITH THE PROPOSED RATE INCREASE OF 51.6 PERCENT.

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<sup>1</sup>H. REPT. 1409, 89th CONG., 2D SESS.

WE BELIEVE THAT THE NO-DEFICIT-YEAR CONCEPT USED IN THE CENTRAL VALLEY PROJECT'S RATE AND REPAYMENT STUDY IS NOT CONSISTENT WITH THE CRITERION USED BY OTHER FEDERAL POWER MARKETING AGENCIES OR WITH CONGRESSIONAL STATEMENTS AS TO THE CONCEPTS WHICH WOULD BE USED IN PREPARING A RATE AND REPAYMENT STUDY.

HYDROLOGY--CONTENTION 2

THE CONTENTION INVOLVING HYDROLOGY IS THAT THE BUREAU UNDERSTATED ESTIMATED FUTURE POWER GENERATION BECAUSE SUCH ESTIMATES WERE BASED ON AVERAGE HYDROGENERATION IN THE LOW-WATER PERIOD 1922-54 RATHER THAN ON LONGER PERIODS.

THE BUREAU ACKNOWLEDGES THAT HISTORICAL RUNOFF FOR THE 1954-71 PERIOD WAS APPRECIABLY GREATER THAN THE AVERAGE RUNOFF DURING THE 1922-54 PERIOD AND SAID THAT THE STUDY WHICH WAS UNDERWAY AT THE TIME OF OUR REVIEW, BUT NOT THEN COMPLETED, WOULD USE UPDATED DATA. ACCORDING TO THE BUREAU'S PRELIMINARY ESTIMATES, INCLUDING THE 1954-71 PERIOD IN THE HYDROLOGY STUDY WOULD SUPPORT AN 8-PERCENT INCREASE IN THE AVERAGE ANNUAL POWER GENERATION BEING USED IN PREPARING RATE AND REPAYMENT STUDIES.

ONE OF THE OPPONENTS OF THE RATE INCREASE HAS ESTIMATED THAT IF HYDROLOGY DATA ALSO WERE INCLUDED BACK TO ABOUT 1895 IT WOULD SUPPORT A 10-PERCENT INCREASE IN THE AVERAGE ANNUAL POWER GENERATION. WE DID NOT EVALUATE THE RELIABILITY OF HYDROLOGY DATA GOING BACK TO ABOUT 1895.

WE ESTIMATE THAT, ON THE BASIS OF THE BUREAU'S STUDY USING UPDATED HYDROLOGY DATA, THE EFFECTIVE RATE FOR BOTH CAPACITY AND ENERGY WOULD

BE APPROXIMATELY 5.97 MILLS PER KWH INSTEAD OF THE PROPOSED 6.15 MILLS PER KWH, AN OVERALL RATE INCREASE OF ABOUT 46 PERCENT COMPARED WITH THE PROPOSED INCREASE OF 51.6 PERCENT.

EARNED SURPLUS--CONTENTION 6

THE CONTENTION INVOLVING EARNED SURPLUS IS THAT THE PROPOSED RATE INCREASE WILL ESTABLISH AN UNJUSTIFIABLE ACCUMULATED EARNED SURPLUS OF \$496 MILLION AFTER PAYMENT OF ALL COSTS, INTEREST, AND AMORTIZATION.

THIS SURPLUS AUTOMATICALLY ACCRUED IN THE RATE AND REPAYMENT STUDY BY 2031 AS A RESULT OF THE BUREAU'S PROPOSING A RATE INCREASE ADEQUATE TO MEET OTHER CRITERIA, PARTICULARLY THAT WHICH PROVIDED THAT THE RATE INCREASE BE ADEQUATE TO AVOID A DEFICIT IN ANY SINGLE YEAR. THEREFORE, ACCORDING TO A BUREAU REGIONAL OFFICIAL, THE SURPLUS DID NOT CONTRIBUTE TO THE PROPOSED RATE INCREASE.

IF THE SURPLUS HAD NOT AUTOMATICALLY RESULTED FROM COMPLYING WITH SUCH OTHER CRITERIA, HOWEVER, THE BUREAU MIGHT HAVE REQUESTED RATE INCREASES ADEQUATE FOR PROVIDING A SURPLUS OF ABOUT \$350 MILLION. THE ORIGINAL BUREAU INSTRUCTIONS FOR PREPARING THE RATE AND REPAYMENT STUDY DIRECTED THAT PROVISION BE MADE FOR A \$350 MILLION SURPLUS. THE BUREAU'S REGIONAL OFFICE RESPONSIBLE FOR ADMINISTERING THE PROJECT STATED THAT SUCH A SURPLUS WAS NEEDED TO COVER CONSTANTLY INCREASING COSTS FOR CONSTRUCTION, OPERATION EXPENSES, AND CONTINGENCIES. ALSO, THE SURPLUS WAS TO PROVIDE ABOUT \$78.4 MILLION TO PAY CERTAIN DEFERRED PROJECT COSTS.

OUR REVIEW OF THE CRITERIA USED BY SOME OF THE OTHER FEDERAL POWER AGENCIES IN PREPARING RATE AND REPAYMENT STUDIES DID NOT DISCLOSE ANY REQUIREMENT FOR A SURPLUS TO COVER INCREASING COSTS OR CONTINGENCIES.

ALSO, THE CRITERIA FOR PREPARING RATE AND REPAYMENT STUDIES, AS SET FORTH IN HOUSE REPORT 1409, 89th CONGRESS, 2D SESSION, DID NOT, IN OUR OPINION, ENVISION THAT PROVISION WOULD BE MADE FOR FUTURE COST INCREASES OR DECREASES. THE HOUSE REPORT STATED THAT FUTURE VARIATIONS WOULD AVERAGE OUT.

ON THE BASIS OF THE RATE AND REPAYMENT STUDY CRITERIA SET FORTH IN THE HOUSE REPORT AND USED BY OTHER FEDERAL POWER MARKETING AGENCIES, WE BELIEVE THAT, EXCEPT FOR PROVIDING \$78.4 MILLION FOR THOSE ITEMS REFERRED TO BY THE BUREAU AS DEFERRED COSTS, POWER RATES SHOULD NOT BE INCREASED TO PROVIDE A SURPLUS.

#### REPLACEMENT COSTS--CONTENTION 7

THE CONTENTION INVOLVING REPLACEMENT COSTS IS THAT SOME OF THE BUREAU'S RATE INCREASE RESULTS FROM EXPENSING SUCH COSTS IN THE YEAR IN WHICH THEY OCCUR RATHER THAN CAPITALIZING SUCH COSTS AND GRADUALLY EXPENSING THEM OVER A NUMBER OF YEARS.

THE BUREAU DID EXPENSE REPLACEMENT COSTS BUT NOW AGREES THAT SUCH COSTS SHOULD BE CAPITALIZED. BUREAU REGIONAL OFFICIALS STATED THAT EXPENSING SUCH COSTS CONTRIBUTED TO THE NEED FOR A RATE INCREASE PRIMARILY BECAUSE OF ANOTHER POLICY USED IN THE RATE AND REPAYMENT STUDY OF NOT ALLOWING A DEFICIT TO OCCUR IN ANY SINGLE YEAR. IF THAT POLICY WERE ELIMINATED, RATES PROBABLY WOULD NOT BE AFFECTED MUCH BY

EXPENSING, RATHER THAN CAPITALIZING, REPLACEMENTS, BECAUSE THE EXPENSE WOULD NOT HAVE TO BE MET IN ANY PARTICULAR YEAR. THIS COULD BE CONCLUSIVELY DETERMINED, HOWEVER, ONLY IF THE BUREAU WERE TO MAKE COMPUTER ANALYSES OF THE RATE AND REPAYMENT STUDIES USING BOTH BASES. WE BELIEVE THAT REPLACEMENT COSTS SHOULD BE CAPITALIZED RATHER THAN EXPENSED IN THE YEAR IN WHICH THEY OCCUR.

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ON NOVEMBER 1, 1973, INTERIOR ANNOUNCED A TWO-STEP RATE INCREASE. ACCORDING TO THE ANNOUNCEMENT, THE FIRST INCREASE, EFFECTIVE APRIL 1, 1974, WILL BE 28 PERCENT; THE SECOND INCREASE, EFFECTIVE JANUARY 1, 1977, WILL BRING THE TOTAL TWO-STEP INCREASE TO APPROXIMATELY THE 51.6 PERCENT ORIGINALLY PROPOSED FOR JANUARY 1974. WE HAVE NOT REVIEWED THE BASIS FOR THIS TWO-STEP INCREASE. OUR REPORT IS CONCERNED ONLY WITH THOSE CONTENTIONS RELATED TO THE BUREAU'S RATE AND REPAYMENT STUDY SUPPORTING THE PROPOSED JANUARY 1974 RATE INCREASE.

THIS CONCLUDES MY PREPARED STATEMENT; WE WILL BE HAPPY TO RESPOND TO ANY QUESTIONS YOU MAY HAVE.

UNITED STATES GENERAL ACCOUNTING OFFICE  
WASHINGTON, D. C. 20548

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SUPPLEMENT TO  
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CHAIRMAN HENRY S. REUSS' LETTER DATED NOVEMBER 20, 1973, TO THE  
COMPTROLLER GENERAL REQUESTED THAT IN ADDITION TO THE MATTERS DISCUSSED  
IN OUR REPORT ENTITLED "CALIFORNIA'S CENTRAL VALLEY PROJECT-PROPOSED  
POWER RATE INCREASE (B-125042 DATED NOVEMBER 19, 1973)", WE SUBMIT ALSO  
A STATEMENT COVERING THE FOLLOWING ADDITIONAL MATTERS.

"1. We understand that the rate increase announced by Interior  
on November 1 for CVP customers is still based on the concepts  
of no-deficit-year, \$496 million surplus, limited (1922-1954)  
hydrology data, and expensing of replacements. If our under-  
standing is accurate, please state, based on your studies,  
whether or not the increase announced by Interior based on those  
factors is warranted."

INFORMATION FURNISHED US BY THE BUREAU OF RECLAMATION SHOWS THAT THE  
RATE INCREASE ANNOUNCED ON NOVEMBER 1 WAS NOT BASED ENTIRELY ON THE CON-  
CEPTS USED IN THE PRIOR RATE AND REPAYMENT STUDY. WE WERE ADVISED BY A  
REGIONAL OFFICIAL THAT THE PRINCIPAL CHANGE FROM THE PRIOR STUDY WAS THAT  
UPDATED HYDROLOGY DATA FOR THE PERIOD 1954-71 WAS USED. USE OF THE RATE

INCREASE ANNOUNCED ON NOVEMBER 1 RESULTS IN THE STUDY SHOWING TWO DEFICIT YEARS AND A SURPLUS OF ABOUT \$579.4 MILLION BY THE YEAR 2031. THIS IS CONTRASTED WITH THE NO-DEFICIT-YEARS AND A SURPLUS OF ABOUT \$496 MILLION SHOWN IN THE PRIOR STUDY.

WE WOULD LIKE TO NOTE THAT IN OUR REPORT TO THE CHAIRMAN, WE POINTED OUT THAT THE POLICY FOR PREPARING RATE AND REPAYMENT STUDIES WAS ANNOUNCED BY THE SECRETARY OF THE INTERIOR IN 1963 AND A CONCISE STATEMENT OF THAT POLICY WAS SET FORTH IN AN APRIL 1, 1966, REPORT BY THE HOUSE COMMITTEE ON INTERIOR AND INSULAR AFFAIRS (HOUSE REPORT 1409, 89TH CONGRESS, 2ND SESSION). WE BELIEVE THAT THE SOLE BASIS INTENDED FOR TESTING THE ADEQUACY OF THE POWER RATE IS CLEARLY STATED IN HOUSE REPORT 1409 AS FOLLOWS:

"As long as the unamortized investment is less than the allowable unamortized investment, this demonstrates that each generating project, and each increment of investment in the transmission system, is being repaid within the allowable period."

OUR SCANNING OF THE REVISED RATE AND REPAYMENT STUDY INDICATES THAT THE RATE INCREASE ANNOUNCED ON NOVEMBER 1, 1973, WAS NOT BASED SOLELY ON THE ABOVE CITED CRITERIA. TO OUR KNOWLEDGE THE BUREAU HAS NOT PREPARED A RATE AND REPAYMENT STUDY USING THE CRITERIA SET FORTH IN HOUSE REPORT 1409. THEREFORE WE ARE UNABLE TO EXPRESS AN OPINION AS TO WHAT POWER RATE INCREASE, IF ANY, IS WARRANTED.

"2. Would suspension of the rate increase until the Department revises its rate and repayment studies with respect to the above four factors be contrary to the public interest? Please explain your reply."

SINCE THE RATE INCREASE ANNOUNCED BY INTERIOR ON NOVEMBER 1, 1973, IS NOT EFFECTIVE UNTIL APRIL 1, 1974, WE BELIEVE THAT AMPLE TIME EXISTS

FOR INTERIOR TO REVISE ITS RATE AND REPAYMENT STUDY BY THAT DATE FOR THE FOUR FACTORS REFERRED TO ABOVE. IN THE EVENT, HOWEVER, THAT INTERIOR SHOULD DECIDE THAT SUCH REVISION OF THE RATE AND REPAYMENT STUDY CANNOT BE ACCOMPLISHED UNTIL AFTER APRIL 1, 1974, A SHORT DELAY IN THE EFFECTIVE DATE OF THE RATE INCREASE WOULD SEEM TO BE JUSTIFIED IN THE INTEREST OF CONSISTENT APPLICATION OF RATE AND REPAYMENT STUDY POLICIES.

"3. The GAO report states (p. 10):

'CVP first began receiving power from the Northwest in January 1972. The power was purchased from the Centralia plant in the State of Washington. For the 18-month period ended June 30, 1973, CVP purchased 382 megawatts of capacity and associated energy (after adjustments for transmission losses) at an average cost of 7.694 mills per kwh.'

What were the 'transmission losses' for this period and what was the cost of these 'losses'?"

BASED ON INFORMATION WE RECEIVED FROM THE BUREAU'S MID-PACIFIC REGION, DURING THE 18-MONTH PERIOD ENDED JUNE 30, 1973, ABOUT 10.5 PERCENT OF THE POWER WAS CONSIDERED UNDER THE TERMS OF APPLICABLE CONTRACTS AS BEING LOST IN TRANSMITTING IT FROM THE CENTRALIA POWER PLANT LOCATED IN WASHINGTON TO THE TRACY LOAD CENTER IN CALIFORNIA. THIS LOSS REPRESENTS ABOUT 808,200 KW/MONTHS OF CAPACITY AND ABOUT 476.8 MILLION KWH OF ENERGY. THE COST OF SUCH TRANSMISSION LOSSES FOR THE PERIOD IS ESTIMATED AT ABOUT \$3.3 MILLION.

"4. The [GAO] report states on page 11 (footnote b):

'There is a single charge for power purchased from the Northwest. CVP allocates the charge between capacity and energy on the basis of formula it devised. If less of the charge were allocated to capacity, the loss from sales to PG&E would be less and the loss on sales to preference customers would be more.'

What is the origin of this formula and how was it developed?"

THE CHIEF, MARKETING AND SALES BRANCH, IN THE BUREAU'S MID-PACIFIC REGION TOLD US THAT HE, IN CONSULTATION WITH OTHER REGIONAL OFFICIALS, DEvised THE ALLOCATION FORMULA AND THAT IT WAS BASED ON THE COMBINED JUDGMENT OF THE REGIONAL OFFICIALS. WE WERE TOLD THAT THIS ALLOCATION WAS MADE INFORMALLY TO SATISFY THE REQUEST FOR SUCH INFORMATION FROM OPPONENTS OF THE RATE INCREASE AND HAD NOT BEEN AGREED TO BY THE PACIFIC GAS AND ELECTRIC COMPANY. THE ALLOCATION IS NOT USED FOR ANY FORMAL ACCOUNTING PURPOSE.

GENERALLY, THE FORMULA PROVIDES FOR THE FOLLOWING ALLOCATION OF THE COST OF NORTHWEST POWER (CENTRALIA POWER PLANT COSTS) BETWEEN CAPACITY AND ENERGY.

	<u>CAPACITY</u>	<u>ENERGY</u>
	-PERCENT-	
FIXED COSTS	100	-0-
OPERATION AND MAINTENANCE COSTS	75	25
FUEL COSTS	10	90

IN ADDITION, WHEELING AND RESERVE COSTS PAID TO THE BONNEVILLE POWER ADMINISTRATION WERE SPLIT BETWEEN CAPACITY AND ENERGY PROPORTIONATE TO THE DIVISION OF CENTRALIA COSTS BETWEEN CAPACITY AND ENERGY. THIS ALLOCATION FORMULA RESULTED IN AN ESTIMATED CAPACITY CHARGE OF \$2.60 PER KW/MONTH AND AN ESTIMATED ENERGY CHARGE OF 5.34 MILLS PER KWH.

WE DISCUSSED THE ABOVE ALLOCATION FORMULA WITH THE CHIEF, DIVISION OF RATES AND CORPORATE REGULATION, FEDERAL POWER COMMISSION (FPC) AND HE ADVISED US AS FOLLOWS:

- A. FPC WOULD NORMALLY CLASSIFY ALL FUEL COST AS ENERGY RELATED, ALTHOUGH, IN SOME CASES, UP TO 5 PERCENT OF FUEL COSTS, IS ALLOCATED TO CAPACITY. THE CENTRALIA POWER PLANT, HOWEVER, OPERATES AT A HIGH LOAD FACTOR SO FUEL COST NORMALLY WOULD BE ALLOCATED ENTIRELY TO ENERGY.
  
- B. FPC NORMALLY ALLOCATES OPERATION AND MAINTENANCE COSTS ON AN ACCOUNT BY ACCOUNT BASIS RATHER THAN A PERCENTAGE BASIS, AND, USUALLY, ALL HEAVY MAINTENANCE IS ALLOCATED TO ENERGY. IN TOTAL, AN EQUAL SPLIT OF OPERATION AND MAINTENANCE COSTS BETWEEN CAPACITY AND ENERGY IS CONSIDERED NORMAL IN MOST CASES, BUT THIS DEPENDS ON THE SITUATION.
  
- C. CAPITAL COST SHOULD BE ALLOCATED ENTIRELY TO CAPACITY.

ALTHOUGH THE INFORMATION WE RECEIVED FROM THE FPC OFFICIAL INDICATED THAT THE FORMULA PREPARED BY THE BUREAU MAY RESULT IN ALLOCATING TOO MUCH OF THE NORTHWEST POWER COST TO CAPACITY, WE DID NOT PURSUE THE MATTER FURTHER BECAUSE THE ALLOCATION IS NOT USED IN THE RATE AND REPAYMENT STUDY OR FOR ANY FORMAL ACCOUNTING PURPOSE.